No. 78-1420

In the Supreme Court of the United States

OCTOBER TERM, 1978

GRUMMAN AEROSPACE CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

WADE H. McCREE, JR.
Solicitor General

BARBARA ALLEN BABCOCK
Assistant Attorney General

BARBARA L. HERWIG
FREDERIC D. COHEN
Attorneys
Department of Justice
Washington, D.C. 20530

In the Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-1420

GRUMMAN AEROSPACE CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Claims (Pet. App. 26a-43a) is reported at 587 F. 2d 498. The opinion and decision of the Armed Services Board of Contract Appeals (Pet. App. 1a-25a) is reported at 75-2 Gov't Cont. Rep. (CCH) BCA para. 11,492.

JURISDICTION

The judgment of the Court of Claims was entered on November 15, 1978. On January 31, 1979, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including March 15, 1979. The petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1255(1).

QUESTION PRESENTED

Whether, in determining the amount due from a government contractor to the United States because state franchise taxes for which the United States had reimbursed the contractor were refunded, the refund should be allocated to the year in which the state franchise tax was initially paid.

STATEMENT

Petitioner is an operating subsidiary of the Grumman Corporation ("Grumman"). In 1966 petitioner's predecessor entered into a contract, known as the EA-6B contract, with the Naval Air Systems Command, calling for the production and modification of certain aircraft (Pet. App. 28a-29a). The original contract was susperseded in 1969 by a "definitized" cost-plus incentive fee contract between Grumman and the United States.[1]

Article 4 of the contract obligated the government to pay the contractor "the cost thereof * * * determined by the Contracting Officer to be allowable in accordance with—(A) Part 2 of Section XV of the Armed Services Procurement Regulation [ASPR] as in effect on the date of this contract; and (B) the terms of this contract * * *" (Pet. App. 37a). ASPR 15. 205-41 provided that taxes were an allowable cost of the contract (Pet. App. 46a). In 1968 Grumman paid a New York State corporation franchise tax of $1,807,870. In accordance with the contract's provisions, the government reimbursed petitioner for the portion of the state franchise tax that was attributable to the EA-

[1]Petitioner assumed the rights and obligations of this contract on June 30, 1969 (Pet. App. 29a).

6B contract (*id.* at 30a). Final delivery on the EA-6B contract was made in March 1970 (*id.* at 29a).

In 1971 Grumman reported a loss that gave rise to a rebate of most of the New York State franchise tax that the company had paid in 1968. The loss was incurred in connection with a contract to provide the government with an aircraft known as the F-14 Tomcat (Pet. App. 30a-31a). New York State law permits a carry-back of net operating losses for a three-year period, and a carry-forward of such losses for a five-year period (*id.* at 29a-30a). On the basis of the carry-back provisions, Grumman filed a "Claim for Credit or Refund of Corporation Tax Paid * * * for period ended December 31, 1968." Grumman received a "credit or refund" of $1,609,000 (*id.* at 32a). and it allocated $1,538,585 to petitioner (*id.* at 33a).[2]

Under the terms of the EA-6B contract, refunds to the contractor of cost items that were originally paid for by the government must be returned to the government. Article 4(f) of the contract provides (Pet. App. 37a):

> The Contractor agrees that any refunds, rebates, credits, or other amounts (including any interest thereon) accruing to or received by the Contractor or any assignee under this contract shall be paid by the Contractor to the Government to the extent that they are properly allocable to costs for which the Contractor has been reimbursed by the Government under this contract.

[2]The tax rebate was allocated to Grumman's various subsidiaries (including petitioner) on the basis of their percentage contribution to the company's total net loss (Pet. App. 32a-33a).

ASPR 15.205-41(c), which is incorporated by reference into the contract, further provides in relevant part (Pet. App. 47a):

> Any refund of taxes, interest, or penalties, and any payment to the contractor of interest thereon, attributable to taxes, interest, or penalties which were allowed as contract costs, shall be credited or paid to the Government in the manner directed by the Government * * *.

In accordance with these agreements, the Defense Contract Audit Agency asserted an entitlement to 39.77% of the 1968 tax refund that was allocated by Grumman to petitioner. That represents the proportion of Grumman's business with the government in 1968 that consisted of cost-type contracts, for which franchise taxes were reimbursed by the government as general and administrative expenses (Pet. App. 8a-9a, 30a, 33a). Petitioner claimed that it was obligated to repay only 14.22% of the tax refund; that percentage corresponded to the percentage of its business accounted for by cost-plus contracts in 1971, the year of the losses that occasioned the tax refund (Pet. App. 9a).

When the disputed amount was not forthcoming, the agency disapproved payment of the contested funds from petitioner's current cost-plus contracts.[3] Petitioner appealed the decision to the Armed Services Board of Contract Appeals, which affirmed (Pet. App. 1a-25a). On petition for review under the standards of the Wunderlich Act, 41 U.S.C. 321-322, in the Court of

[3]The disputed funds associated with the EA-6B contract amount to $90,737 (Pet. App. 33a).

Claims, that court granted the government's motion for summary judgment and dismissed petitioner's claims (Pet. App. 26a-43a).

Both the Board and the Court of Claims rejected petitioner's argument that the payment was not a "refund" of the 1968 tax, which would be governed by Article 4(f) of the contract, but rather an economic subsidy. They concluded that the state itself referred to the repayment as a refund, as did other authorities (*e.g.*, Rev. Rul. 65-190, 1965-2 Cum. Bull. 150) on which petitioner relied (Pet. App. 21a-23a, 41a-42a). The Board then concluded, and the Court of Claims agreed, that the terms of the contract, and the ASPR provisions that it incorporated, require allocation of the refund to the 1968 tax payments for which petitioner had been reimbursed by the United States. They noted that Article 4(f) of the contract, and the ASPR cost principles that it incorporates, " 'are concerned with assuring that if the Government pays a cost and later that cost is reduced, by whatever means, the Government receives the benefit of that reduction' " (Pet. App. 23a-24a, 40a). Only allocating the refund to 1968 will achieve this result (*ibid.*).

Because the contract's language governs, the Court of Claims considered it unnecessary to determine whether, as petitioner argued, the refund would be allocated to 1971 for federal income tax accounting purposes (Pet. App. 43a).

ARGUMENT

Petitioner renews in this Court its arguments that generally accepted accounting principles require allocation of the tax refund to 1971, the year of the losses that occasioned the refund (Pet. 13-15), and that state tax policy is frustrated by any other result (Pet. 15-17).

It also argues (Pet. 9-12) that allocation to 1968 is precluded by provisions of ASPR itself, which explicitly incorporate generally accepted accounting principles as the method of allocating costs under the contract.[4]

Petitioner is correct in noting (Pet. 11) that a number of ASPR provisions (*e.g.*, Section 15.201-15. 201-2, 15.201-4 and 15.203 (texts at Pet. App. 45a-46a)) refer to generally accepted accounting principles as a means of determining proper allocation of costs. But these provisions deal generally with initial determination of costs, not with allocation of refunds. Refunds are addressed elsewhere (see Article 4(f) of the contract, *supra;* ASPR 15.205-41(c), *supra*), and these more specific provisions necessarily govern. The Court of Claims' interpretation of those provisions involves no issue of general importance, and thus there is no reason for review by this Court.

Whatever the usual financial accounting or tax accounting treatment of state tax refunds may be,[5] the contract makes it clear that, if the government reimburses the contractor for the contractor's tax payments and the tax is later reduced "by whatever means," the government will receive the full benefit of that reduction. *RMK-BRJ,* ASBCA No. 16031, 74-1 Gov't Cont. Rep. (CCH) BCA para. 10,535 at 49,896.

---

[4]Petitioner also argued below that the government was estopped from allocating the income tax credit to 1968. This argument was rejected by the Court of Claims (Pet. App. 33a-37a) and is not renewed here.

[5]Cf. *Thor Power Tool Co.* v. *Commissioner,* No. 77-920 (Jan. 16, 1979) (generally recognized accounting principles do not control the availability of loss writedowns for income tax purposes).

See also *Northrop Aircraft, Inc.* v. *United States*, 127 F. Supp. 597, 599 (Ct. Cl. 1955); *Northrop Corp.*, ASBCA No. 8502, 1964 Gov'ts Cont. Rep. (CCH) BCA para. 4102.[6] Petitioner's contention, by contrast, necessarily leads to the conclusion that if, in the year that the losses were incurred, the contractor no longer had any cost-plus contracts, the government would receive no reimbursement even if all of the tax payments were refunded. This is not what the parties contemplated when they agreed that "[*a*]*ny* refund of taxes * * * shall be credited or paid to the Government in the manner directed by the Government." ASPR 15.205-41(c) (emphasis added).[7]

Petitioner's contention that the decision below fails to give effect to state tax policy also ignores the terms of the contract. Whatever state tax policy might be, petitioner agreed to return to the United States any tax refunds it received. It thereby surrendered, as a condition of the contract, any state-conferred benefit.

---

[6]In *Northrop Corp.* a Renegotiation Board decision in 1958 had the effect of reducing Northrop Corporation's income for 1955. As a result, Northrop received a refund of the state franchise tax it paid in 1956. The Board of Contract Appeals held that the refund constituted a reduction of 1956 costs, and that the government, under its cost-plus contract, was entitled to share in the refund to the extent that it had reimbursed the contractor for such costs. "We interpret the contract clauses * * * as obligating appellant to refund to the Government contracting agency under the cost reimbursement type contracts the same percentage of the California State franchise tax refund as was paid by the Government as reimbursement of administrative overhead pool for appellant's fiscal year ended 31 July 1956." *Id.* at 20,030.

[7]Since the contract made it clear that the 1968 refund would have to be used to reimburse the government for payments made on 1968 taxes, petitioner's claim (Pet. 12) that its expectations were frustrated is without basis.

At all events, the contention that the state tax refund was intended as a subsidy to petitioner is insubstantial. The payment is designated by the state as a refund, not a subsidy, and loss carry-back provisions are not a form of financial assistance to business. Rather, such provisions are designed to ensure that companies whose incomes are the same over an extended period will be subject to equal tax burdens. *Libson Shops, Inc.* v. *Koehler*, 353 U.S. 382, 386 (1957). The Court of Claims' decision here does not interfere with the State's attempt to equalize the amount of New York franchise tax paid by petitioner and other corporations doing business in that state. It simply requires that, once the state tax burden has been adjusted, the company reimburse the government so that the government will not have paid the contractor for costs that the contractor ultimately does not incur.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

WADE H. MCCREE, JR.
Solicitor General

BARBARA ALLEN BABCOCK
Assistant Attorney General

BARBARA L. HERWIG
FREDERIC D. COHEN
Attorneys

MAY 1979

DOJ-1979-05